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No. 96-44

IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

CMC HEARTLAND PARTNERS,

Petitioner,

v.

UNION PACIFIC RAILROAD COMPANY,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

SUPPLEMENTAL BRIEF FOR PETITIONER

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This supplemental brief responds to the Brief for the United States as Amicus Curiae.

The Solicitor General concedes that "[p]etitioner may be correct that the split of authority precipitated by *Frenville* presents an issue of general importance under the bankruptcy laws." U.S. Br. at 18. Yet because the Solicitor General apparently endorses the result below and the *Frenville* analysis on which it is based, *see id.* at 14-15 & 16 n.4, he goes to great lengths to avoid review here.

1. The Solicitor General first echoes respondent's argument that this Court should deny *certiorari* on the ground that the question presented to this Court is framed more broadly than the issue decided by the courts below. *See* U.S. Br. at 10-13. Like respondent, the Solicitor General emphasizes that the second round of litigation below focused on the narrow question whether the liability imposed by Washington's MTCA was analogous to the liability imposed under prior state law. *See id.* at 11.

As petitioner has already explained, the narrow focus of the second round of litigation was ordained by the Court of Appeals' disposition of the first round of litigation. *See* Pet. Rep. at 6-7. During that first round, petitioner advanced the very argument it advances here—that a federal bankruptcy "claim" can arise even before a state-law cause of action has accrued if the *facts* on which the claim is based are known. *See id.* at 6 (quoting petitioner's appellate briefs).[1]

It is hardly surprising, thus, that the Solicitor General carefully refrains from endorsing respondent's mistaken

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[1] The Solicitor General half-heartedly attempts to explain away one of the passages cited by petitioner from its first-round briefs below, *see* U.S. Br. at 13 n.2, but makes no effort to explain away the other passage, *see* Pet. Rep. at 6. In any event, these incomplete explanations fail to recognize that throughout this litigation petitioner has sought to formulate several related arguments to support its position, both challenging and seeking to distinguish the cases relied on by the court below.

contention that petitioner failed to preserve below the issue presented here. Rather, the Solicitor General asserts only that petitioner's *legal arguments* with respect to that issue now sweep more broadly than before. Even if that assertion were correct (which it is not), the Solicitor General recognizes that it would not preclude this Court's review of the question presented. *See* U.S. Br. at 12-13. The Solicitor General's invocation of amorphous "prudential concerns" to avoid review ignores the fact that the legal and factual issues presented in the petition are fully developed and ripe for review.

Indeed, the Solicitor General acknowledges that the Seventh Circuit *expressly addressed* the very issue presented for review. *See* U.S. Br. at 6 (noting that the Seventh Circuit concluded in the first round of litigation that "'Union Pacific's claim for indemnification of its liability under state law arose after the discharge and thus was not barred'") (quoting Pet. App. at 23a); U.S. Br. at 9 (noting that the Seventh Circuit stated in the second round of litigation that its prior decision had "'joined other courts * * * in concluding that claims based on a statute enacted after the discharge date are not barred'") (quoting Pet. App. at 3a). It is unquestionably appropriate for this Court to review an issue that the court below actually addressed. *See, e.g., Lebron v. National R.R. Passenger Corp.*, 115 S. Ct. 961, 965 (1995).

2. On the merits of the question presented—whether a State can frustrate a federal bankruptcy discharge by imposing new post-discharge liabilities based on known pre-discharge conduct—the Solicitor General's brief only confirms the need for this Court's review. In endorsing the Seventh Circuit's reasoning and result, the Solicitor General tacitly endorses the approach previously adopted by the Third Circuit in *In re Frenville Co.*, 744 F.2d 332 (3d Cir. 1984), *cert. denied*, 469 U.S. 1160 (1985), which has been roundly criticized by courts and commentators for more than a decade. *See* Pet. at 13-15 &

nn. 12, 13. The Solicitor General offers three arguments in support of his position.

First, the Solicitor General asserts that the term "claim" as used in federal bankruptcy law is not broad enough to encompass post-discharge state-law liabilities based on pre-discharge conduct. *See* U.S. Br. at 13-14. He thus echoes a similar position unsuccessfully advanced by the United States in such previous cases as *Pennsylvania Dep't of Public Welfare v. Davenport*, 495 U.S. 552 (1990), and *Ohio v. Kovacs*, 469 U.S. 274 (1985), where this Court emphasized that the term "claim" must be given its broadest possible definition to resolve all conceivable liabilities in a bankruptcy discharge. *See Davenport*, 495 U.S. at 558; *Kovacs*, 469 U.S. at 279; *see also Johnson v. Home State Bank*, 501 U.S. 78, 83 (1991).[2]

Second, the Solicitor General observes that many provisions of federal bankruptcy law incorporate state law by reference. *See* U.S. Br. at 14-15. That observation, however, misses the point. It is one thing for the federal bankruptcy laws to look to state law to determine the legal consequences of pre-discharge conduct in a federal bankruptcy discharge; it is another thing altogether for state law to create or alter rights or obligations based on pre-discharge conduct *after* the discharge.[3]

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[2] Unlike respondent, the Solicitor General acknowledges that, at least for purposes of this case, there is no meaningful difference between the definition of "claim" in § 77 of the Bankruptcy Act of 1898 and the 1978 Bankruptcy Code. *See* U.S. Br. at 14. Petitioner has already explained why this is so. *See* Pet. Rep. at 2-3; *see also Gardner v. New Jersey*, 329 U.S. 565, 573 (1947) ("[T]he sweeping, all-inclusive definitions of 'claims' and 'creditors' in § 77 leave no room for exception under it.").

[3] The Solicitor General's attempt to analogize this case to cases involving post-discharge liabilities created under *federal* law only confuses the issue. *See* U.S. Br. at 16 & n.4 (citing *In re Chateaugay Corp.*, 53 F.3d 478 (2d Cir.), *cert. denied*, 116 S. Ct. 298 (1995)); *In re Penn Central Transp. Co.*, 944 F.2d 164 (3d Cir. 1991), *cert. denied*, 503 U.S. 906 (1992). Petitioner

(continued...)

Third, the Solicitor General asserts that the federal bankruptcy laws present no obstacle to the imposition under state law of "retrospective liability on all persons who engaged in similar conduct during a defined time period," even if such persons have undergone a reorganization and received a federal bankruptcy discharge. U.S. Br. at 16 n.4. With all due respect, this position ignores the Supremacy Clause. It is well-established that the federal bankruptcy laws preempt inconsistent state enactments. *See, e.g., Stellwagen v. Clum*, 245 U.S. 605, 613 (1918). Once a reorganized entity has received a federal bankruptcy discharge, it is treated, for federal bankruptcy purposes, as a *new and distinct entity* that does not carry forward any liabilities and obligations from the pre-petition entity.[4] That is the essential foundation of the "fresh start" policy embodied in federal bankruptcy law—a critical point that underscores the importance of the issue presented here. *See* Memorandum to the Solicitor General from Prof. Elizabeth Warren 3-4 (Nov. 6, 1996) (attached as Appendix A). The Solicitor General may sympathize with state environmental laws that "complemen[t]" the federal environmental laws, U.S. Br. at 16 n.4, but such state laws cannot preempt federal bankruptcy law.

3. Finally, the Solicitor General mimics respondent's efforts to negate the circuit split by artificially narrowing the question presented in this case. Like respondent, the Solicitor General contends that the only question presented is whether a state

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[3] (...continued)
has never challenged the authority of Congress to enact federal statutes that limit the scope of the federal bankruptcy laws. *See* Pet. at 13 n.11. The issue in this case is not whether one federal statute trumps another, but whether state law will be allowed to trump federal law.

[4] Thus, the proper analogy here is not between a reorganized entity and all other businesses, but between a reorganized entity and all other businesses *that commenced operations on or after the date of the federal bankruptcy discharge.*

statutory cause of action that arises after a federal bankruptcy discharge may be applied to pre-discharge conduct. A state *common-law* cause of action that arises after a federal bankruptcy discharge, the Solicitor General insists, presents a "distinct" issue. *See* U.S. Br. at 17. This is the quintessential distinction without a difference.[5]

For federal bankruptcy purposes, it is immaterial why, in any particular case, a cause of action arises *after* the underlying conduct on which it is based. It may arise by virtue of the enactment of a new statute, or it may arise by virtue of a host of other "future event[s]." U.S. Br. at 18. The Solicitor General offers no reason why a post-discharge cause of action based on the common law may be characterized as "contingent," but a post-discharge cause of action based on a statute may not. There are any number of reasons why a given cause of action may not arise until long after the facts on which it is based—the maturation of a loan guaranty, the prolonged latency period of an illness, the creation of a new employee right, the enactment of a new statute, or a change in substantive common-law rights (*e.g.*, an expansion of successor liability). In each of these instances, and many others, allowing new post-discharge claims under state law would threaten the central objectives of the federal bankruptcy laws—equal treatment of all creditors and a "fresh start" for the reorganized entity.

Thus, the Solicitor General's effort to narrow the question presented in this case rests upon nothing but the same semantic sleight-of-hand previously attempted by respondent. The Solicitor General's assertion that the cases criticizing *Frenville* all involved a "cause of action that was in existence at the time

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[5] Indeed, so desperate is the Solicitor General to narrow the question presented that he actually declares that "there is little likelihood that a conflict will develop among the courts of appeals over the question whether the MTCA creates new liability distinct from prior state law." U.S. Br. at 17.

of the bankruptcy," U.S. Br. at 18, is untrue in all but in the most theoretical sense. *None* of those causes of action was in existence at the time of the bankruptcy; none of them had accrued until subsequent developments that postdated the bankruptcy discharge. Indeed, they might never have accrued, just as the Washington state legislature might never have enacted the MTCA; they were not simply "unripe," but again, there was *no* "existing cause of action at the time of the bankruptcy." *Id.* The crucial point is that none of these subsequent events, whatever their significance under state law, can be allowed to trump a federal bankruptcy discharge in a closed case.

The Solicitor General also attempts to deny the circuit split by emphasizing that the Seventh Circuit did not cite *Frenville* below. *See* U.S. Br. at 18. That is true but irrelevant, as the Seventh Circuit *did* apply *Frenville*'s reasoning. Instead of citing *Frenville* directly, the Seventh Circuit cited another Third Circuit case, *In re Penn Central Transp. Co.*, 944 F.2d 164 (3d Cir. 1991), *cert. denied*, 503 U.S. 906 (1992), which in turn relied on *Schweitzer v. Consolidated Rail Corp.*, 758 F.2d 936 (3d Cir.), *cert. denied*, 474 U.S. 864 (1985), which in turn relied on *Frenville*. *See* App. at 33a, 3a; 944 F.2d at 167-68; 758 F.2d at 943. The Solicitor General implicitly acknowledges that *Penn Central* is aligned with those cases (which he favors) that accord with and descend from *Frenville*. *See* U.S. Br. at 16-18. That point has been underscored by the Third Circuit itself, which in the second round of the *Penn Central* litigation expressly relied on *Frenville* and pointedly reaffirmed its continued adherence to the *Frenville* analysis, despite its recognition of the mounting criticism from other courts. *See In re Penn Central Transp. Co.*, 71 F.3d 1113, 1117 n.5 (3d Cir. 1995), *cert. denied*, 116 S. Ct. 1851 (1996).

By adopting the *Frenville* analysis in this case, the Seventh Circuit has now intensified the existing circuit split. As the Solicitor General concedes, the Fourth and Ninth Circuits have

expressly rejected *Frenville* and held that a federal bankruptcy discharge bars a subsequent state-law claim when "the potential claimant has sufficient notice" of the pre-petition conduct so that the potential liability is within the parties' "fair contemplation" at the time of the bankruptcy. *See* U.S. Br. at 17-18 (citing *In re Jensen*, 995 F.2d 925, 930-31 (9th Cir. 1993); *Grady v. A.H. Robins Co.*, 839 F.2d 198, 201-03 (4th Cir.), *cert. dismissed*, 487 U.S. 1260 (1988)). If the Seventh Circuit had followed this analysis, rather than the *Frenville* approach, petitioner would have readily prevailed in light of the manifest environmental problems at the Tacoma railyard that doomed respondent's attempt to circumvent the bankruptcy discharge with its CERCLA claims. Similarly, the Solicitor General acknowledges that the Eleventh Circuit has expressly rejected *Frenville* and held that a federal bankruptcy discharge bars a subsequent state-law claim wherever there is "a significant pre-petition relationship between the debtor and the potential claimant." *See* U.S. Br. at 17 (citing *In re Piper Aircraft Corp.*, 58 F.3d 1573, 1577 (11th Cir. 1995)). If the Seventh Circuit had applied this test, rather than the *Frenville* approach, petitioner would again have readily prevailed in light of respondent's extensive involvement in the Milwaukee Road bankruptcy. Notwithstanding the Solicitor General's semantic contortions, the fact thus remains that the result in this case would have been different had it been filed in these other circuits—the very definition of a circuit split.[6] This particular

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[6] *See also Franklin Sav. Ass'n v. Office of Thrift Supervision*, 31 F.3d 1020, 1022 (10th Cir. 1994) (noting the "split in authority regarding when a right of payment of an unmatured claim arises for bankruptcy purposes"); *In re Hemingway Transp., Inc.*, 954 F.2d 1, 8 n.9 (1st Cir. 1992) (refusing to follow *Frenville* and noting that "more recent decisions consistently have declined to accept the *Frenville* reasoning and its failure to accord full breadth to the term 'claim'"). The Bankruptcy Courts are also split over *Frenville*. *Compare In re Barrett*, 136 B.R. 387, 395 (Bankr. E.D. Pa. 1992); *In re Adams*, 106 B.R. 811, 823 (Bankr. N.J. 1989) *with In re Fairchild Aircraft Corp.*, 184 B.R. 910, 923 (Bankr. W.D. Tex. 1995); *In re*

split is especially undesirable, as it encourages forum-shopping under the federal bankruptcy laws, where the Constitution specifically seeks the establishment of "uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8, cl. 4.

4. Although the Solicitor General endorses the decision below and urges this Court to deny review, he does not deny the practical significance of this case. Indeed, even if the Solicitor General were correct that the question presented here could reasonably be limited to the validity of state attempts to impose new *statutory* (as opposed to *common law)* liability based on pre-discharge events, the issue is still of immense importance. The Solicitor General's brief takes no account of numerous letters that he received from entities that currently are or previously were involved in a bankruptcy reorganization. Such of those letters as petitioner has been able to obtain are attached as Appendix B. The letter from the American Financial Group, in particular, notes that the company has invested "hundreds of millions of dollars in reorganizing companies" over the past thirty years, but will not continue to invest in reorganizing businesses until this disparate application of the bankruptcy laws is righted, because investors cannot now "rely on the finality of discharge and a fresh start for the debtor." *See* App. at 11a. These letters vividly illustrate the harm wrought by decisions like the one below and *Fremville*, and underscore the need for this Court to address and clarify this unsettled corner of the law.

5. There is yet another reason why the issue raised in this case is of substantial importance to the lives of millions of Americans and to the United States Treasury. The Pension

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Edge, 60 B.R. 690, 704 (Bankr. M.D. Tenn. 1986). The latter split alone is enough to warrant this Court's review of this important federal bankruptcy issue. *See, e.g., Davenport*, 495 U.S. at 557 ("To address a conflict among Bankruptcy Courts on this issue, we granted *certiorari* . . . . ").

Benefit Guaranty Corporation, created by Congress in 1974, is an independent federal agency entrusted with insuring and protecting the pension benefits of more than 30 million Americans who work in the private sector and their dependents. *See PBGC v. LTV Corp.*, 496 U.S. 633, 636-40 (1990). The PBGC plays an increasingly important role in many corporate reorganizations. *See, e.g.*, Daniel Keating, *Chapter 11's New Ten-Ton Monster: The PBGC and Bankruptcy*, 77 Minn. L. Rev. 803 (1993). In its petition for *certiorari* in the *LTV* case, which itself arose out of a prolonged Chapter 11 proceeding, the PBGC noted that it deals regularly with bankrupt employers and "has a docket of more than 600 active bankruptcy cases." Petition for Certiorari in *PBGC v. LTV Corp.*, U.S. No. 89-390, at 26.[7]

As shown in an accompanying memorandum that petitioner has compiled from public sources, the PBGC has become a direct stakeholder with substantial equity interests in a number of reorganized entities. *See* Appendix C. Thus, for example, the PBGC received a $375 million general unsecured claim in the Continental Airlines bankruptcy settlement, which was satisfied by the issuance of common stock in the reorganized entity. Similarly, in the Kaiser Steel bankruptcy proceeding, the PBGC became a 28% shareholder in the reorganized company, and in the TWA bankruptcy proceeding, the PBGC received notes payable by the reorganized company worth a total of $244 million as well as more than four million shares of common stock. These examples and the others set forth in Appendix C show that the PBGC has a direct and very substantial interest in maintaining the integrity of the federal bankruptcy process against the imposition of new state-law

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[7] Congress has granted the PBGC its own independent litigating authority, *see* 29 U.S.C. § 1302(b)(1), so that the Solicitor General is neither under any obligation nor in a position to recognize and represent the PBGC's important interests in the bankruptcy issue raised in this case.

liability based on based on pre-discharge events. The PBGC thus shares the same interest as potential investors and reorganized companies in ensuring that—in *all* circuits, not just in some—a bankruptcy discharge provides the essential "fresh start" at the heart of the federal bankruptcy laws.

6. The decision below poses a fundamental threat to the efficiency and integrity of the federal bankruptcy process. The Seventh Circuit held, and respondent and the Solicitor General agree, that petitioner is subject to potentially enormous liability for conduct by its predecessor that occurred years *before* a federal bankruptcy discharge under a state statute that was not enacted until years *after* the discharge. The decision below thus allows state law to circumvent the discharge and thereby to undermine the constitutionally-rooted uniformity of the federal bankruptcy laws. This Court should resolve the circuit split presented in this case by firmly rejecting any such notion of "reverse preemption."

CONCLUSION

The petition for writ of *certiorari* should be granted.

Respectfully submitted,

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APPENDIX A

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DATE: November 6, 1996

RE: Petition for Certiorari for CMC Heartland Partners v. Union Pacific Railroad Company

I have no doubt that every party who comes to the Justice Department asking for help persuading the Supreme Court to grant certiorari argues that the legal issue presented to the court is of the utmost consequence. In this case, however, the claim that the disputed legal issue relates to the very heart of an important part of the legal system is not even a slight exaggeration. The extent to which a bankruptcy filing resolves all the claims based on the debtor's pre-filing past is a question that goes to the essence of what bankruptcy should accomplish.

The Seventh Circuit opinion in *CMC Heartland Partners v. Union Pacific Railroad Company*—like that of the Third Circuit in *In re Frenville Co.*—sharply narrows the range of options available to a bankrupt business to deal with all the parties who may claim its assets. If allowed to stand, the implications of these decisions of failing businesses, for those who are trying to put the assets of those businesses back into productive use, for those who face uncompensated injuries, and for those who have other claims against the business are profound. This is not a simple case of debtor versus creditor, a decision in which favoring one party necessarily injures

another. Instead, this is question about the scope of the bankruptcy laws, about whether they provide a final opportunity to separate the activities of the debtor's pre-bankruptcy past from those of its post-bankruptcy future, and whether all claimants from that past have a right to treatment on an equal footing. When a broad question of scope has been raised by the circuit courts, it deserves the timely attention of the Supreme Court. This is particularly so where, as here, there is a growing conflict among the circuits on the proper resolution to that question.

In this case, long after the Milwaukee Railroad (predecessor in interest to CMC Heartland) filed its bankruptcy and confirmed a plan of reorganization, Union Pacific Railroad is now alleging that it has a right to collect on its pre-bankruptcy indemnification claim. toxic spills—and had a full opportunity to participate in the bankruptcy which it took advantage of, the company claims that the indemnification obligation survived. According to Union Pacific, the only obligations that were discharged in bankruptcy were those indemnification claims it might assert under the laws as they stood at the moment of the bankruptcy discharge. The Seventh Circuit agreed, holding that any new legal basis for liability against a party to whom the debtor once owed indemnification, such as the passage of another environmental law, was adequate to revive the moribund indemnification claim. If this view of claims revival stands, any change in status that creates a new payment obligation for beneficiaries of indemnification, such as a change in state caselaw or statutory law, creates a new claim against a post-bankruptcy entity. This result threatens the essence of a bankruptcy discharge.

Background: The Claims Process in the Bankruptcy System

A few years ago, I was asked by the Federal Judicial Center to write a summary of the operation of the business bankruptcy system, explaining the most important features in non-technical language for use by the non-specialist federal

courts. In the resulting book,[1] which was reviewed by judges throughout the federal system before publication, claims are featured prominently in the first substantive chapter. I explain the starting point of bankruptcy law for both liquidations and reorganizations:

> A profound shift in the relationship between debtors and creditors occurs at the filing of a bankruptcy petition. A new estate is created, comprising both the legal and economic interests of the old debtor and the collective economic and legal interests of the creditors. Creditors lose their individual collection rights against the debtor, and they are forced to deal with an estate operating on behalf of all the creditors.[2]

This fundamental shift is captured more vividly in the claims process:

> The transformation of claims against a debtor into claims against an estate protects the collective nature of the bankruptcy proceeding. By converting creditors' claims against the pre-bankruptcy debtor to claims against a bankruptcy estate, the Code gives the estate manager a position to account for, to monitor, and to value each charge against the estate's assets.[3]

The extent to which the bankruptcy system forces all parties who may call on the debtor for payment into a collective proceeding is governed by the interpretation of the claims provisions first in the Act in section 77 and then in the

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[1] Elizabeth Warren, *Business Bankruptcy* (Federal Judicial Center 1993).

[2] *Id.* at 61.

[3] *Id.* at 61-62.

Code in section 101(5). If this provision is given a narrow reading, the impact on the bankruptcy process is profound: bankruptcy will deal with less than all of the obligations arising from the pre-bankruptcy behavior of the debtor. If the provision is read broadly, then a bankruptcy case may reasonably deal with all the obligations incurred by the debtor, creating a cleavage between the debtor's pre-filing past, which will be dealt with collectively, and the debtor's post-filing future, in which parties may deal individually with the surviving entity.

The practical implications of this difference are enormous. If an obligation of the debtor is not dealt with in the bankruptcy, then the obligation may survive after the bankruptcy case is completed. In some cases, this means that creditors who have a claim tied to the debtor's pre-bankruptcy past may disrupt the debtor's post-bankruptcy future. A claimant who is not dealt with in the collective bankruptcy proceedings, for example, and whose claim is therefore not processed and paid on par with other claimants, may come back to the surviving business after a plan is confirmed to assert claims for compensation that disrupt the post-filing debtor's business.

The Importance of this Issue to the Bankruptcy System

The question of what claims shall be covered in a bankruptcy proceeding involves the distributional issues at stake in any bankruptcy action:

> The claims process is critical to the distributional objectives of the Code. As claims are estimated, valued, and assigned certain priority rights, the distributional scheme of the bankruptcy system comes to life. Whether an obligation owed by a debtor becomes a claim—and can thus be discharged—raises a critical distributional question among competing creditors. Similarly, the discharge of claims or the rewriting of payment

> obligations over time necessarily distributes the assets of the estate among competing parties.[4]

If a creditor is denied the opportunity to participate in a final distribution by a failing debtor, the Bankruptcy Code fails to deliver its promised equality of treatment. Similarly, if a creditor can profit from reserving some part of its claim and later collect more from the surviving business, the distributional goal of equality of treatment among creditors is also violated.

A corollary to the equality-of-distribution argument is the reinvestment argument. A principle function of bankruptcy is to preserve the going concern value of a failing business, permitting the business to remain intact rather than to be liquidated for pro rata distribution to its creditors. The creditors of the failing business must be paid at least as much as they would have gotten in the liquidation (a requirement of § 1129(a)(9)), and the going-concern premium can fund higher payments. The business, and the jobs it supplies, can be preserved without imposing additional injury on the creditors. A large part of preservation of going-concern value depends on new capital investment. New money can flow into a business only if the new investors can be certain that old liabilities have been identified and dealt with.

One reason the bankruptcy laws use a very expansive definition of "claim" is to resolve ALL claims—potential and actual, matured and unmatured, contingent and non-contingent, liquidated and unliquidated. If there were unresolved claims outstanding, then new investments in the failing business would be sharply curtailed. Investors would buy assets at lower prices from liquidation sales rather than invest in reorganizing businesses.

In the late 1980s, I engaged in a lengthy debate with Professor Douglas Baird about bankruptcy policy.

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[4] *Id.* at 61.

Notwithstanding our differences on a number of points about striking the appropriate balance between debtors and creditors, we agreed on the critical importance of including all parties who may raise a claim against a debtor for its pre-filing behavior in a single bankruptcy action:

> The bankruptcy system equalizes the treatment of creditors and parties affected by business failure when timing variations leave them with very different formal rights. . . . The Code generally minimizes the consequences of timing differences among the debtor's prepetition creditors as it reorders claims based on an underlying similarity of rights. [footnote omitted][5]

Any decision, such as those in *CMC Heartland* and *Frenville*, that leaves the new business with the risk of unknown, unquantifiable losses that may arise in the future directly undercuts the ability of the business to reorganize in bankruptcy, to maximize its returns to its unpaid creditors and to survive as an employer. If a shift in state law suddenly imposes new losses on a business long after its reorganization is complete, the cost of investing in bankrupt business has just risen sharply.

One final point about the impact of a decision about when a bankruptcy claim arises is in order. That question is implicated in the most difficult cases facing the courts over the next dozen years. Environmental claims, product liability claims, and mass tort claims, for which we have currently only seen the tip of the iceberg, are multiplying against American businesses. A significant number of those businesses will find their way into the bankruptcy courts in the next two decades. At the same time, emerging business practices mean that large

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[5] Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 Mich. L. Rev. 336, 358-59 (1993).

business purchases are now routinely accompanied by indemnification clauses, so that all companies—including those facing financial difficulties—are more likely to have a collection of outstanding indemnification obligations. If the Seventh Circuit opinion in *CMC Heartland v. Union Pacific* stands, every change in state law that alters the potential responsibility of a party—extensions of statutes of limitations, expansions in the sweep of liability principles, development of third-party liabilities—will threaten to unravel bankruptcy reorganizations long-since thought to be settled. Financial reorganization of complex entities will become almost impossible.

If hastily made judicial decisions constrain the reach of the bankruptcy system to deal with the problems identified here, it will be no victory for judicial economy. Instead, decisions creating false boundaries that limit which claims can be collectively treated in a bankruptcy case will spawn countless more cases, as parties dispute whether their particular facts fall inside or outside the newly modified claims definition. Moreover, parties will spend the intervening time maneuvering for position in and out of the bankruptcy system rather than submit their difficulties to a single forum for a unified resolution. Variations in state law, rather than uniform interpretation of the federal bankruptcy laws, will dominate the system. Only by keeping the scope of bankruptcy discharge orders broad, as Congress intended and as the Supreme Court has thus far consistently ruled, can bankruptcy serve as a forum to resolve multiple disputes without expending endless resources on disputes about whether the proceedings include all the disputants.

The kinds of obligations drawn into the bankruptcy process as claims against the estate powerfully affect both the collective nature of the bankruptcy proceedings and the distributional impact of bankruptcy. The lines that are drawn to determine which obligations are included within the bankruptcy discharge are the lines that determine whether the

bankruptcy goals of equality of treatment among creditors and preservation of the going concern value of a business can be realized.

Any decision that limits the scope of bankruptcy discharge orders has a powerful impact on the bankruptcy system. Such a decision will constrain the ability of the parties to settle all disputes related to a debtor's pre-bankruptcy past in a single forum. It will encourage both strategic behavior and multiple lawsuits. It will undermine the central principle of the federal bankruptcy laws—to treat like claimants alike—leaving those with pre-filing injuries to a collective treatment in the bankruptcy proceeding while those whose injuries arise later founder alone, sometimes receiving much better subsequent treatment and other times receiving no compensation at all.

I urge the Justice Department to support the granting of the Petition for Certiorari in *CMC Heartland Partners v. Union Pacific Railroad Company*. The issue will not disappear, and continued uncertainty and division among the circuits will only heighten the costs imposed on all the parties who are trying to deal with claims against a failing company.

APPENDIX B

AMERICAN FINANCIAL GROUP

November 15, 1996

VIA FAX: 202-514-9769
AND EXPRESS MAIL

Walter E. Dellinger
Solicitor General of the United States
Department of Justice
950 Pennsylvania Avenue, NW
Washington, DC 20530-0001

Re: Petition for Certiorari: CMC Heartland Partners v. Union Pacific Railroad Company, Supreme Court No. 96-44

Dear General Dellinger:

I write at this time to urge you to support the granting of certiorari in the referenced matter. This case raises an issue which has enormous repercussions for companies like ours that regularly invest in reorganizing companies. Over the last 30 years our company has invested hundreds of millions of dollars in reorganizing companies. We were willing to make such investments in reliance upon the fact that the bankruptcy would discharge claims arising from the preconsummation conduct of the debtor. Unfortunately, in light of the Seventh Circuit's decision in *CMC Heartland* and the Third Circuit's decisions in *In re Frenville* 744 F.2d 332 (3d Cir. 1984) *cert. denied* 469 U.S. 1160 (1985) and its progeny, similar investments now are not only imprudent but dangerous. These decisions undermine the fundamental bankruptcy principles of finality and fresh start and allow claims to remain pending as a sword hanging over the reorganized company and its new investors. Until

these erroneous decisions are corrected, our company will not invest in reorganizing businesses.

Our concerns are not imaginary or hypothetical. Today our company is defending itself from the threat of serious financial loss as a result of the Third Circuit's jurisprudence in this area which, like the Seventh Circuit in *CMC Heartland*, erroneously narrows the scope of a bankruptcy discharge contrary to the express intent of Congress. The Third Circuit cases in question—*In re Penn Central Transportation Co.* (Paoli Yard), 944 F.2d 164 (3d Cir. 1991) *cert. denied* 503 U.S. 906 (1992) and *In re Penn Central Transportation Co.* (USX) 71 F.3d 1113 (3d Cir. 1995), *cert. denied* 116 S. Ct. 1851 (1996)—involved our subsidiary, The Penn Central Corporation (n/k/a American Premier Underwriters, Inc.). *Paoli Yard* involved a CERCLA claim to recover environmental remediation costs and *USX* involved a contribution claim to recover antitrust damages. In both cases there was no dispute that the alleged conduct giving rise to the claims was conduct of the debtor, not the reorganized company, and that all of this conduct occurred prior to consummation. Indeed, the alleged offending conduct in both cases began in the 1950's, more than 20 years before consummation and nearly 40 years before claims were asserted against the reorganized company. Nevertheless, the Third Circuit, applying the same erroneous definition of when a claim arises as the Seventh Circuit, ruled that the reorganized company could be held liable for claims arising from the preconsummation conduct of the debtor. Obviously, our company as a new investor in the reorganizing debtor had no knowledge of, involvement with or control over such conduct.

The Third and Seventh Circuit jurisprudence obliterates well-established bankruptcy policies of finality and fresh start. These courts have judicially determined (contrary to legislative intent) that massive claims can survive consummation and discharge. Consequently, our subsidiary, the reorganized company, is now defending itself from over $700 million in

claims arising exclusively from the preconsummation conduct of the debtor. It is especially egregious that the result in every circuit other than the Third and Seventh would be the opposite—these claims would have been found to have been discharged. Until this disparate application of the bankruptcy laws is righted, investors will not take a stake in reorganizing companies because they cannot rely on the finality of discharge and a fresh start for the debtor.

Very truly yours,

/s/Carl H. Lindner

CHL/hkc

GREENBERG
ATTORNEYS AT LAW
TRAURIG

Peter M. Gillon
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PRIVILEGED & CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

November 13, 1996

The Honorable Walter Dellinger
Solicitor General of the United States
Office of the Solicitor General
U.S. Department of Justice
Washington, D.C. 20530

Re: CMC Heartland Partners v. Union Pacific R.R.
U.S. No. 96-44

Dear Mr. Solicitor General:

It has come to our attention that the Supreme Court has asked the Solicitor General to state the views of the United States about whether the Court should take review of the *CMC Heartland Partners* case on an important issue at the intersection of bankruptcy and environmental law. On behalf of Continental Airlines, Inc., a former chapter 11 debtor, I urge the Solicitor General to respond in favor of review.

The issue in this case is an important one for former chapter 11 debtors such as Continental Airlines. The issue is the effectiveness of the discharge obtained under the Bankruptcy Code against causes of action newly minted under state law but premised on conduct occurring prepetition. From Continental's standpoint, any uncertainty as to the scope of the discharge obtained by chapter 11 debtors upon confirmation of a plan of reorganization is undesirable.

Having emerged from bankruptcy in 1993, Continental Airlines has proven to be one of the more successful chapter 11 reorganizations in recent years. Under Continental's plan of reorganization, unsecured creditors received a combination of cash and shares of common stock. Continental's common stock has increased in value eight-fold since the plan became effective. The reaction of the stock market to CAL's successful reorganization would likely have been far less enthusiastic (and creditors who continued to hold stock would have been far less fortunate) if the discharge in bankruptcy were not effective as to all claims. The possibility that discharged liabilities could be resuscitated by the acts of a state or local legislative body would have created significant uncertainty as to the company's liabilities and presented unknown risks to investors in the company, to the detriment of the company, its employees and its shareholders.

Because these concerns raise important public policy issues regarding the uniform federal application of the Bankruptcy Code, the Solicitor General has an important stake in the outcome of this case. The United States also has an interest in preserving the effectiveness and finality of the bankruptcy discharge as a creditor asserting claims against debtors throughout the country. That is true for two reasons. First, the decision in this case allows state and local governments to create false priorities that in effect trump the priority of unsecured creditors such as the United States. Second, through the Pension Benefit Guaranty Corp., the Internal Revenue Service, the Environmental Protection

Agency, the Department of the Interior, and other federal agencies, the United States has asserted claims in bankruptcy against numerous chapter 11 debtors, resulting in the distribution to the United States of shares of common and preferred stock in the reorganized company. Allowing states to circumvent the bankruptcy discharge could reduce the value of such holdings.

Finally, there is the issue of delay. In many cases, final distributions to creditors under confirmed plans of reorganization are withheld until all claims have been resolved. Uncertainty as to liabilities that may be imposed makes it exceedingly difficult for a chapter 11 debtor to close out the bankruptcy process. The result of such uncertainty could be a delay in payments to creditors and an open-ended, Dickensian bankruptcy process.

For these reasons, I urge the Solicitor General to support the granting of the Petition for Certiorari in *CMC Heartland Partners*. What is sorely needed in this complex area of law is more uniformity, more certainty, and more clarity. That need raises an issue of national interest deserving of the Court's involvement.

Thank you for your consideration in this matter.

Very truly yours,

/s/Peter M. Gillon
Peter M. Gillon

PMG/mar
cc: Jennifer L. Vogel
Vice President, Legal
Continental Airlines, Inc.

AVATAR HOLDINGS INC.

November 18, 1996

The Honorable Walter Dellinger
Solicitor General of the United States
Office of the Solicitor General
U.S. Department of Justice
Washington, D.C. 20530

Re: CMC Heartland Partners vs. Union Pacific R.R. U.S. No. 96-44

Dear Mr. Solicitor General:

In my capacity as General Counsel for Avatar Holdings Inc. f/k/a the GAC Corporation, I am forwarding this letter to you to address the pending *CMC Heartland Partners* case. The sole issue in the case as presented before the United States Supreme Court is when a "claim," as defined for purposes of the federal bankruptcy laws, will be deemed to arise in a federal bankruptcy proceeding when the underlying cause of action is based on state law. This issue is one of great importance to many of the reorganizations, including the reorganization involving Avatar Holdings Inc., that are regularly effected under federal law. In light of the fact that the Supreme Court has asked the Solicitor General to state the views of the United States about whether the Court should take review of this issue on the merits and settle it conclusively as a matter of federal bankruptcy law, I am hereby urging you to respond in favor of the Court rendering a decision on this important issue.

I have reviewed the Memorandum of Kirkland & Ellis forwarded to you dated November 5, 1996, and the

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Memorandum referenced therein prepared by Professor Elizabeth Warren dated November 6, 1996, and I am totally in agreement with the reasoning, problems and implication issues expressed therein. Continued uncertainty in this area will hamper reorganizations by leaving all the entities involved uncertain about whether the central aims of the federal bankruptcy laws will be met in their particular circumstances. One of the main, if not the main, objectives of the Congress in enacting the Bankruptcy Code were to provide for an equitable and comprehensive settlement of the outstanding debts and to allow the debtor to reorganize and thereby achieve a "fresh start" that will allow the underlying businesses to continue in operation, which benefits all of their stakeholders, including employees, customers, and suppliers, rather than pushing them into liquidation. If, as in the *CMC Heartland Partners* case, a reorganized entity can be subjected to liability under state law years after a federal court had granted a federal bankruptcy discharge, based on a new statutory cause of action, then it is clear that the congressional intent embodied in the Bankruptcy Code has been substantially overridden. This unfortunate situation not only will cause great and unwelcome uncertainty by creating a new cloud over federal bankruptcy proceedings, but it will also be unfair to previous creditors whose debts were discharged for lesser amounts and to new creditors who have agreed to invest in the reorganized entity on the understanding that the federal bankruptcy discharge was effective for its intended purposes.

Further, the consequences of this issue are not limited simply to cases of environmental claims, though they are certainly one example of the kinds of situations in which the issue may arise. Instead, this issue has potential significance for all manner of corporate reorganizations or state statute. It also will affect corporate reorganizations where various causes of action do not arise until after the bankruptcy discharge because the underlying conduct did not immediately result in actionable injury, as typically occurs in mass tort cases. In light of recent experience with Chapter 11 proceedings, this means that the

issue of when a claim will be deemed to arise under federal bankruptcy law when the underlying cause is based on state law is of tremendous significance and merits a clear and controlling disposition by the Supreme Court at the earliest possible time. I therefore urge you to suggest that the Supreme Court should seize the opportunity to address this issue in the pending *CMC Heartland Partners* case.

In 1976, the GAC Corporation n/k/a Avatar Holdings Inc. commenced bankruptcy reorganization proceedings in the United States District Court Southern District of Florida and these proceedings concluded in 1981. At that time, this was the biggest bankruptcy in the history of the State of Florida and, to the best of my knowledge, still is the biggest. Therefore, you can understand the extent and potential ramification which this issue could have on Avatar Holdings Inc. as the reorganized company. Rather than get into a long dissertation thereon, it should suffice to say that this issue is considered of paramount importance and that Avatar Holdings Inc. feels strongly that the merits of this issue should be reviewed by the Supreme Court.

Thank you for your attention to this important matter.

Very truly yours,

AVATAR HOLDINGS INC.

/s/ Dennis J. Getman
Dennis J. Getman
General Counsel

DJG/ps

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November 20, 1996

The Honorable Walter Dellinger
Solicitor General of the United States
Office of the Solicitor General
U.S. Department of Justice
Washington, D.C. 20530

Re: CMC Heartland Partners v. Union Pacific Railroad, U.S. No. 96-44

Dear Mr. Solicitor General:

I write in reference to the above case. The issue before the United States Supreme Court is to determine the scope of a federal bankruptcy discharge as applied to state-law claims that did not even arise until after the bankruptcy proceeding had already been completed.

This issue is significant for the success of any reorganization. In fact, Uniroyal Technology Corporation is the product of a reorganization under Chapter 11 of the U.S. Bankruptcy Code in which there were a number of environmental issues. If claims had been permitted to arise anew after the bankruptcy process had run its course, the success of the reorganization would have been seriously jeopardized.

I understand that the Supreme Court has formally sought the views of the United States about whether the Court should decide this issue on full review in this case. We request that you advise the Court to do so. Continued ambiguity on

this issue will impede reorganizations by undercutting Congress's main purposes as embodied in the bankruptcy laws. Congress plainly intended to ensure each debtor a fresh start that would enable the business to survive as a going concern and to continue serving its investors and customers, rather than disrupting them all by forcing them to participate in a liquidation of the business. The Uniroyal Technology case is a useful example of the balancing of the interests of all the interested parties, all of whom received something; businesses that had good reason for continued existence were allowed to survive and provide continued employment for over one thousand employees.

If, as in the *CMC Heartland Partners* case, a reorganized entity can be subjected to prepetition liability under state law based on a new statutory cause of action even years after a federal court had granted a federal bankruptcy discharge, then the clear intent of Congress is not being upheld by the courts. This situation also threatens to disrupt the system of treating all unsecured creditors on an equal basis by allowing the new claimants to recover more on their claims than all other claimants were permitted to recover in the now-closed bankruptcy proceeding.

It would appear that the effects of the *CMC Heartland Partners* case are not limited to environmental claims but to any claims that could arise under state law. Such a consequence is clearly inconsistent with the main purposes of the Bankruptcy Code.

In the case of the bankruptcy reorganization resulting in the creation of Uniroyal Technology Corporation, the final Plan of Reorganization was the product of a delicate balance of claims by, among others, suppliers, bondholders, federal and state claimants in respect of approximately twenty superfund sites, the Pension Benefit Guaranty Corporation in respect of an underfunded pension plan and retiree medical claimants. This reorganization, which resulted in the U.S. EPA and the PBGC taking major stock positions in the new company, would

not have been possible if the various claimants had believed that the resolution of claims was not to be final and the reorganized entity was to be subject to later prepetition claims asserted by other creditors. In addition, the financial interests of both federal agencies would have been disserved in the circumstances of the ruling review in the *CMC Heartland Partners* case.

We therefore request that you advise the Supreme Court to seize the opportunity to address this issue in the *CMC Heartland Partners* case. Thank you.

Very truly yours,

/s/ Oliver J. Janney
Oliver J. Janney

OJJ:rah

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Lloyd M. McBride
1934-1983

Edward H. Baker, Jr.
1935-1970

November 12, 1996

Honorable Walter Dellinger
Solicitor General of the United States
Officer of the Solicitor General
U.S. Department of Justice
Washington, DC 20530

Re: *CMC Heartland Partners v. Union Pacific R.R. Co.* U.S. Supreme Court No. 96-44

Dear Mr. Solicitor General:

As counsel to Taracorp, Inc., we have recently been made aware of the fact that your office has been asked by the Supreme Court for its views in connection with a pending petition for *certiorari* filed in this matter. The issue presented to the Court involves the question of when a "claim" under the federal bankruptcy laws will be deemed to arise for purposes of discharge when the underlying cause of action is founded on state law. This issue is significant to many bankruptcy reorganizations, including that of our client, Taracorp, and we strongly believe that the Solicitor General should support review by the Court.

Until the Court decides the issue raised in this case, existing and future bankruptcy proceedings will be unnecessarily hindered. It is clear that Congress' primary purpose in enacting the Bankruptcy Code was to provide for a

comprehensive resolution of the debtor's liability, and to thereafter insure a "fresh start" so that the debtor could continue in business for the benefit of all those persons economically dependent upon its continuing viability, rather than be forced to liquidate to pay its creditors. In *CMC Heartland*, the Court of Appeals for the Seventh Circuit held that an entity reorganized under the bankruptcy laws may yet be subjected to liability under state law notwithstanding bankruptcy discharge, where the claim is based upon a state statute enacted after the bankruptcy concluded. We believe that this decision ignores the substantial Congressional intent reflected in the Bankruptcy Code that debtors should be afforded a fresh start following an equitable distribution of assets to their creditors. This will not occur if prepetition facts can be the basis for non-discharge liabilities based upon state statutes enacted after the debtor's exit from bankruptcy.

Taracorp's experience demonstrates that this concern is not merely hypothetical. Taracorp entered Chapter 11 bankruptcy in 1982. Prior to that time, Taracorp operated secondary lead smelting and fabricating facilities as it continues to do today. Many of the activities commonly employed in the secondary lead business, which occurred before CERCLA became law in 1980, involved the potential for releases of lead and other hazardous substances to the environment; notwithstanding that such activities complied with then-applicable law. Moreover, CERCLA, and statutes like it have been interpreted to have retroactive effect, and attribute liability on a far-broader basis than prior law. For example, in 1979, Taracorp became party to a spent battery "tolling agreement" with Union Scrap Iron & Metal Company, a scrap metal processor in Minneapolis. Union Scrap's services for Taracorp involved processing spent lead-acid batteries to recover scrap lead, which was subsequently shipped to Taracorp. Taracorp ceased doing business with Union Scrap in 1981 and emerged from reorganization in 1985. In 1990, the United States commenced an action against Taracorp and other defendants who had sent spent batteries for

processing by Union Scrap. The allegations against each defendant were that it had "arranged for" the treatment or disposal of a hazardous substance (*i.e.*, lead) by Union Scrap, and therefore was responsible to the United States for costs of remedying the environmental contamination caused by Union Scrap.

Although Taracorp ultimately settled the Unites States' claims against it, the action is illustrative of the problems faced by entities which have emerged from bankruptcy. In this regard, Taracorp's present circumstances are strikingly similar to those of the Petitioner in *CMC Heartland Partners*. Under the Seventh Circuit's interpretation, Taracorp would remain liable for environmental response costs attributable to pre-bankruptcy contamination under any post-1985 statute which might impose such liability, thus impairing Taracorp's "fresh-start" and post-bankruptcy viability.

We urge the Solicitor General to suggest to the Court that review in this case is appropriate to resolve these vitally important issues. Thank you for your attention.

Very truly yours,

/s/Clifton A. Lake
Attorney for TARACORP, INC.

127541

UNR Industries, Inc.

332 S. Michigan Avenue
Chicago, Illinois 60604
Phone 312 341 1234
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Victor E. Grimm
Vice President
General Counsel &
Corporate Secretary

November 15, 1996

The Honorable Walter Dellinger
Solicitor General of the United States
Office of the Solicitor General
U.S. Department of Justice
Washington, D.C. 20530

RE: CMC Heartland Partners v. Union Pacific R.R.
U.S. No. 96-44

Dear Mr. Solicitor General:

The pending *CMC Heartland Partners* case has recently been brought to our attention. As you know, the issue in the case as presented before the United States Supreme Court is when a "claim," as defined for purposes of the federal bankruptcy laws, will be deemed to arise in a federal bankruptcy proceeding when the underlying cause of action is based on state law. The issue posed is one of great importance to many reorganizations under federal law. We understand that the Supreme Court has now asked the Solicitor General to state the views of the United States as to whether the Court should review this issue.

We urge you to request that the Court grant the review petition. Continued uncertainty concerning claims under the

Bankruptcy Code will hamper reorganizations by leaving all the entities involved uncertain of the consequences of reorganization under the federal bankruptcy laws. The main objectives of Congress is enacting the Bankruptcy Code provisions concerning reorganizations were to provide for an equitable and comprehensive settlement of all claims and to allow the debtor to achieve a "fresh start" by allowing the underlying business to continue in operation to the benefit of stakeholders, including employees, customers, lenders and suppliers. If, as in the *CMC Heartland Partners* case, a reorganized entity can be subjected to lability under state law years after a federal court had granted a federal bankruptcy discharge based on a new statutory cause of action, then the congressional intent embodied in the Bankruptcy Code will have been substantially undermined. This unfortunate situation not only will cause great uncertainty by creating a new cloud over federal bankruptcy proceedings, but it will also be unfair to previous creditors whose debts were discharged for lesser amounts and to new creditors and investors who have relied on the discharge of previous debts provided by the Bankruptcy Code.

The experience of UNR with reorganization proceedings confirms the importance of the bankruptcy issue raised in this case. UNR Industries, Inc. was reorganized under the Bankruptcy Code in 1989. Under the Plan of Reorganization, 63% of the stock of the Company was transferred to the UNR Asbestos-Disease Claims Trust. The beneficiaries of the Trust are persons with asbestos disease claims based upon exposure to asbestos manufactured by predecessor companies. If state statutes could create new causes of action based on past conduct, a reorganized company such as UNR could be severely threatened and the individual asbestos claimants deprived of compensation for their claims.

Thank your for your consideration in this matter.

Yours very truly,

/s/Victor E. Grimm
Victor E. Grimm

VEG:bfk

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November 8, 1996

The Honorable Walter Dellinger
Solicitor General of the United States
Office of the Solicitor General
U.S. Department of Justice
Washington, D.C. 20530

RE: CMC Heartland Partners v Union Pacific R.R. U.S. No. 96-44

Dear Mr. Solicitor General:

The pending *CMC Heartland Partners* case has recently been brought to our attention. As you know, the sole issue in the case as presented before the United States Supreme Court is when a "claim," as defined for purposes under the federal bankruptcy laws, will be deemed to arise in a federal bankruptcy proceeding when the underlying cause of action is based on state law. The issue posed is one of great importance to many of the reorganizations that are regularly effected under federal law. We understand that the Supreme Court has now asked the Solicitor General to state the view of the United States about whether the Court should take review of this issue on the merits and settle it conclusively as a matter of federal bankruptcy law.

We urge you to respond in favor of the Court rendering a decision on this issue in this case. Continued uncertainty on this point will hamper reorganizations by leaving all the entities involved uncertain about whether the central aims of

the federal bankruptcy laws will be met in their particular circumstances. · The main objectives of the Congress in enacting the Bankruptcy Code were to provide for an equitable and comprehensive settlement of outstanding debts and to allow the debtor to reorganize and thereby achieve a "fresh start" that will allow the underlying businesses to continue in operation, which benefits all of their stakeholders, including employees, customers, and suppliers, rather than pushing them into liquidation. If, as in the *CMC Heartland Partners* case, a reorganized entity can be subjected to liability under state law years after a federal court had granted a federal bankruptcy discharge, based on a new statutory cause of action, then it is clear that the congressional intent embodied in the Bankruptcy Code has been substantially overridden. This unfortunate situation not only will cause great and unwelcome uncertainty by creating a new cloud over federal bankruptcy proceedings, but it will also be unfair to previous creditors whose debts were discharged for lesser amounts and to new creditors who have agreed to invest in the reorganized entity on the understanding that the federal bankruptcy discharge was effective for its intended purposes.

The experience that we have had with reorganization proceedings confirms the general importance of the bankruptcy issue raised in this case. AM International, Inc. has been through two reorganization proceedings under Chapter 11 of the Bankruptcy Code. We believe that to permit a State to create new liabilities based upon prepetition activities, by enacting new statutes after confirmation, would circumvent the discharges obtained in these proceedings, is contrary to the intent of Congress, and jeopardizes the fresh start provided by the discharge orders. A definitive ruling by the Supreme Court is necessary to prevent potential abuse of the bankruptcy process by the States.

The consequences of this issue are not limited to environmental claims, though they are certainly one example of the kinds of situations in which the issue may arise. Instead, this issue has

potential significance for all manner of corporate reorganizations where new causes of action may be created after the bankruptcy discharge because the underlying conduct did not immediately result in actionable injury, as typically occurs in mass tort cases. In light of recent experience with Chapter 11 proceedings, this means that the issue of when a claim will be deemed to arise under federal bankruptcy law when the underlying cause of action is based on state law is of tremendous significance and merits a clear and controlling disposition by the Supreme Court at the earliest possible time. Therefore, we urge you to suggest that the Court should review and address this issue in the pending *CMC Heartland Partners* case.

Thank you for your consideration in this matter.

Very truly yours,

/s/David L. Rutherford
David L. Rutherford
Associate General Counsel

APPENDIX C

Debt & Equity Distributions to Agencies of the Federal Government in Significant Chapter 11 Cases

The United States has multiple interests in reorganization cases under the bankruptcy laws. In all cases, it has an interest in seeing to it that Congress' twin goals—an equitable distribution to claimants and the creation of a viable new entity—are achieved. In many bankruptcies, however, the United States has an additional interest as a direct stakeholder in the reorganized entity. A number of government agencies, including the EPA, IRS, and, most prominently, the PBGC, regularly file claims against companies in bankruptcy reorganization cases, on account of which they receive debt, stock or some other interest in the reorganized entity—including, at times, a substantial equity interest. Those direct financial interests could be adversely affected to a significant degree by the *Frenville* and *CMC Heartland* approach to post-discharge claims.[1] Petitioner has not yet had a full opportunity to pull together all such situations. Nonetheless, information with respect to some is set forth below.

1. ***In re Continental Airlines Holdings, Inc. et al.***, Case No. 90-0093, etc. (Bankr. D. Del.). Pursuant to a settlement, the PBGC received a $375 million general unsecured claim, which was divided into four classes: Class A: $241.0 million; Class B: $103.1 million; Class C: $12.9 million; and Class D: $18.0 million. Each class received varying amounts of shares of Reorganized Continental

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[1] Indeed, one such situation is ubiquitous and built into the statute itself. Under 11 U.S.C. § 1129(a)(9)(C), a debtor is authorized to stretch out payment of prepetition current tax claims, including those of the IRS, over a period as long as six years. The prospect that the IRS would actually receive eventual payment of tax claims under the terms of this statutory provision would be undermined if new post-discharge claims could be asserted against the reorganized entity.

("NewCal") Class A and Class B Common Stock. In addition, pursuant to a settlement with the PBGC and the IRS, NewCal agreed to issue 415,000 to 580,000 shares of New Cal common stock to the Continental Airlines Retirement Plan.

2. ***In re Trans World Airlines, Inc.***, Case No. 95-43748 (Bankr. E.D. Mo.). Pursuant to TWA's plan, the PBGC received, on account of its claim of approximately $345 million, three notes of the reorganized company in the aggregate amount of $244,344,987 and 4,166,167 shares of Common Stock.

3. ***In re Kaiser Steel Corp.***, Case No. 87 B 1552 (Bankr. D. Colo). The PBGC became a 28% shareholder of the reorganized company.

4. ***In re LTV Corporation, et al.***, Case Nos. 86B 11270-11334, etc. (Bankr. S.D.N.Y.). There are four things worth noting. First, the EPA was entitled to a general unsecured claim of $32.6 million for CERCLA cleanup costs ($28.2 million) and natural resource damages ($4.4 million). This claim entitled the EPA to participate in a pool representing 15.9% to 19.5% of New LTV common stock and 18.2% to 22.1% of reorganized LTV Steel common stock. Second, the PBGC received, as part of a settlement with the debtors, Stock Appreciation Rights entitling the PBGC to receive shares of New LTV common stock. Third, New LTV agreed, as part of the PBGC settlement, to issue $126 million of its common stock to its pension plans and to make annual $30 million contributions to the plans from 1992-1997, and $50 million thereafter. Fourth, pursuant to a settlement agreement, the IRS received, among other things, New LTV common stock with a value of $6.5 million.

5. ***In re CF&I Steel Corp.***, Case No. 90B-6721 (Bankr. Utah). Pursuant to the plan of reorganization, substantially all of the debtor's assets were purchased by a partnership in which the PBGC owned a 4.8 % limited partnership interest. A unit of Oregon Steel Mills Inc. owned

the remaining 95.2% general partnership interest. The PBGC had filed claims totaling approximately $337 million.

6. ***In re Wheeling-Pittsburgh Steel Corp.***, Case No. 85-793-4297 (Bankr. W.D. Pa.). Pursuant to the reorganization, the PBGC reeived on its pension claim, among other things, a six-year note in the face amount of $12 million issued by the reorganized company, payable in annual installments of $2 million; the IRS received on its pension tax claim, among other things, a similar six-year note in the face amount of $11 million issued by the reorganized company, payable in annual installments of $1,833,333.

7. ***In re E-II Holdings, Inc.***, Case No. 92-B-43614 (Bankr. S.D.N.Y.). Pursuant to the debtor's plan, the PBGC received a 10-year unsecured note accruing interest at 11.5%. The principal amount of the note is determined according to a formula and appears to be substantial.

8. ***In re Farley Inc***. Pursuant to its plan, the debtor agreed to make 20 quarterly payments of $125,000 to its various PBGC-guaranteed pension plans.

9. ***In re Amdura Corporation***, Case No. 90B-3811E-3816E (Bankr. D. Colo.). The PBGC received an unsecured debenture in the principal amount of $3 million with interest at 1½% over Continental Bank's reference rate, payable over seven years.

10. ***In re Insilco Corporation***, Case No. 91-70021 (Bankr. W.D. Tex.). The EPA received $10 million, half of which was to be paid in stock of the reorganized company, pursuant to a settlement of a $900 million CERCLA claim. (The balance was to be paid in cash from an insurance litigation recovery.) The Deputy Chief of the Environmental Enforcement section, Joel Gross, who presided over this settlement, indicated that the stock would eventually be sold to pay for cleanup activities at Insilco sites.

11. ***In re Eagle-Picher Industries Inc.***, Case No. 1-91-00100 (Bankr. S.D. Ohio). The EPA received a general

unsecured claim totaling approximately $41 million, a penalty claim of $1.1 million (75% of which was subordinated), and an administrative claim of $150,000. The Eagle-Picher Plan contemplates that the EPA will receive, on account of these claims, a pro rata share of a pool of cash, notes, and stock of the reorganized Company.

12. ***In re National Gypsum Co.***, Case No. 390-37213-SAF-11 (Bankr. N.D. Tex.). The EPA received, on account of a $10.1 million cleanup and natural resource damages claim, senior notes, common stock, and warrants of the reorganized company having an estimated aggregate value of $3.3 million.

13. ***In re Uniroyal Technologies, Inc., et al.***, Case No. 91-32791, etc. (Bankr. N.D. Ind.). The EPA (along with Indiana and Wisconsin) agreed to accept stock in settlement of CERCLA claims. Stipulation provides that when particular environmental liabilities of a particular debtor in the Uniroyal Group become fixed, that debtor is given the option of paying the amount in cash, or by distributing its equity securities that have a value equivalent to the fixed amount of the liability.

14. ***In re Munsingwear***, Case No. 4-91-4581 (Bankr. D. Minn.). Pursuant to the debtor's plan the PBGC received stock in the reorganized company of approximately $2 million on account of its claim of approximately $23 million..